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C O N F I D E N T I A L SECTION 01 OF 03 ACCRA 000636

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TAGS: ENRG EFIN EINV GH
SUBJECT: AMBASSADOR PRESSES PRESIDENT KUFUOR TO SUPPORT CMS ENERGY PROJECT

Classified By: EconChief Chris Landberg for Reasons 1.5 (B and D)

Summary

¶1. (C) Ambassador Bridgewater met March 15 with President Kufuor to urge his support for CMS Energy's $200 million project to expand its thermal power plant in Ghana from 220 MW to 330 MW. CMS and the IFC-led lenders group have failed so far to convince Cabinet to approve the government guarantee of the loan. Kufuor said he was willing to work with CMS and IFC to reach an agreement, but did not accept the lenders' current conditions. In a separate meeting on March 14, Ambassador D.K. Osei, Secretary to the President, commented that the President has serious reservations about CMS, because he believes it has "taken Ghana to the cleaners." We explained that the expansion is a win-win deal for Ghana, but Ghanaian officials are unconvinced and appear swayed by influential CMS opponents. President Kufuor agreed to meet a high-ranking CMS official next week to discuss the matter further. We understand CMS will also be lobbying in Washington, leading up to President Kufuor's April 12 meeting with President Bush. Post will continue efforts to build support in Cabinet. End Summary.

President Kufuor's Perspective

¶2. (C) Kufuor confirmed his staff's earlier warnings to Emboffs that he is skeptical and has a negative view of both the current take-or-pay agreement with CMS and the proposed expansion. Kufuor noted with irritation that both then-Secretary of State Colin Powell and President Bush raised CMS in their first ever meetings, and this clearly put CMS in his bad graces (Note: the Powell and Bush comments related to Ghana's arrears to CMS in 2002-2004. End Note). He dismissed EconChief's argument that the expansion would increase power generation, lower electricity costs, and ensure Ghana takes full advantage of the West Africa Gas Pipeline (WAGP), and thus was a win-win deal for Ghana. He argued instead that for years Ghana had paid CMS enormous sums for expensive electricity, and "got nothing out of it." He strongly opposed the current terms of the IFC-led loan, and stated that IFC would have to renegotiate before he would support the deal. (Note: The CMS plant is expensive due to high world oil costs and the high-risk investment environment. The expansion will increase output by 50% with zero additional fuel costs, leading to lower cost electricity. End Note).

¶3. (C) The Ambassador pressed Kufuor on the benefits of the deal and exhorted him to meet with IFC and CMS to find a way forward. She noted that CMS's President for Enterprises, Tom Elward, planned to visit Ghana next week, and urged Kufuor to meet with him. Kufuor relented a little as the meeting ended, emphasizing that he was open to discussion and meeting with Elward, and agreed the deal could be important for Ghana.

President Aide's Negative Appraisal of the Deal
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¶4. (C) Osei painted a more negative picture during his earlier meeting with the Ambassador, arguing that most Cabinet Ministers disagreed with the entire premise that the expansion was good for Ghana. He added that even if CMS satisfied the President's own concerns, he would hesitate to override the entire Cabinet. Osei stated that CMS's only two supporters in the Cabinet, Energy Minister Mike Ocquaye and Senior Minister J.H. Mensah, had acquitted themselves poorly in explaining the deal during Cabinet meetings. In particular, they did not explain how this deal was superior to other options, or why the government should be required to take on the contingent liability when the loan was to CMS. Osei added that for many Ministers this was a matter of national pride. They are fed up with donor demands after years of IMF and World Bank conditionality and suffering through the humiliation of HIPC debt relief.

¶5. (C) Osei argued his own view that CMS received an excessive rate of return and charged too high a price to VRA for electricity. He claimed power plants in Senegal, Benin and Cote d'Ivoire were much cheaper, and the "Spanish and Italians" had offered much better terms to build plants in Ghana. He also argued for exploring hydropower options.

Osei disregarded EconChief's argument that the lenders' independent consultants has concluded that the contract price was reasonable and the least cost available power generation alternative open to Ghana. He also disagreed with the argument that CMS's return rate was high because it was first to market and faced higher risks, or that the way to lower rates was to attract more investors and increase competition. He even argued that Ghana already produced plenty of power to meet its future needs, despite overwhelming evidence to the contrary. Osei rejected the argument that risks are high in Ghana, and argued that Ghana had developed past the point where investors and lenders should expect higher returns than elsewhere. (Comment: These remarks are Osei's, but we suspect that there are key members of Cabinet who share these sentiments. End Comment).

Background on CMS Expansion

¶6. (C) CMS Energy invested $100 million equity in 1998 to install two 110 MW combustion turbine generators near the Takoradi Port. CMS partnered with VRA (which invested $10 million), forming the Takoradi International Company (TICO). The goal was for CMS to duplicate VRA's own 330 MW plant, which is co-located with TICO. CMS planned to install a 110 MW steam or "second cycle," which would be driven by the exhaust of the 220 MW TICO plant, representing a 50 percent increase in output with no increase in fuel costs. Economic conditions and inadequate electricity tariffs delayed the project until 2004, when the IFC agreed to lead a lenders consortium for the $215 million loan.

IFC and other Lenders' Concerns and Loan Conditions
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¶7. (C) Since government-owned VRA is the sole purchaser of power, the lenders have so far insisted on certain conditions, including a government guarantee. IFC and CMS have been unable to overcome widespread opposition in Cabinet to the guarantee. IFC's other requirements, which focus on ensuring VRA's financial stability, are proving even more controversial.

¶8. (C) The lenders are concerned about VRA's ability to keep up payments to CMS because of its subsidy to Valco, the aluminum smelter the GoG purchased from Kaiser Aluminum and reopened at partial capacity last year. At the direction of President Kufuor, VRA charges Valco only 2.7 cents/kwh, but VRA's power costs are near 5 cents/kwh. Therefore, the lenders have insisted that the GoG agree to fund the anticipated gap in VRA's revenues) estimated between $40 and $70 million in 2006. (Note: other, less objectionable IFC conditions relate to foreign exchange risks and power sector reorganization. End Note).

¶9. (C) According to local CMS officials, IFC has shown some flexibility in recent meetings with VRA officials, and is exploring alternatives to its demands for GoG payments to VRA. (Comment: this is appropriate; the GoG will have to fund the projected Valco revenue gap, regardless of whether there is a written commitment to IFC. End Comment).

Background on Ghana's Power Needs

¶10. (C) Ghana nominally produces approximately 1700 MW of electricity, with over 1200 MW from Akosombo Dam and the rest from the VRA and CMS petroleum-powered plants. It also imports electricity from natural gas-powered plants in Cote d'Ivoire. While this covers current demand, it will not once Valco comes fully online and the Newmont mines begin operations. Newmont will require 75 MW of power, and Alcoa, should it go forward with preliminary plans to mine bauxite and build an alumina refinery, would need roughly an equivalent amount. Furthermore, Volta lake levels have fallen to dangerously low levels, forcing VRA to rely less on cheap hydro power and more on the expensive VRA/CMS plants. Also, the VRA thermal power plant is poorly run and has an average availability rate of well below 50% (compared to the CMS plant's 80-90% availability rate). While WAGP will lower costs for thermal power from VRA and CMS once it comes online in December 2006, it is a take-or-pay arrangement and the CMS expansion dramatically improves the financials. (Note: WAGP gas will be equivalent to dropping the fuel price from over $60/barrel to under $25/barrel. Given that VRA expects to import almost $200 million more in petroleum in 2006, just for the VRA/CMS plants, WAGP will result in huge savings. End Note).

Comment

¶11. (C) Ambassador Osei's comments are not unexpected. CMS considers him an adversary, who together with others in the GoG) including the Chief of Staff) have attempted to undermine CMS since the Kufuor government took over in 2001. This group is in league with the controversial and notoriously corrupt ex-VRA Chief Wareko Brobby, whom Kufuor removed in 2003 following a series of scandals and death threats from VRA workers. CMS suspects Brobby may be behind

the disinformation campaign that many Cabinet members seem to have bought on to. Local CMS officials claim that Brobby, Osei, and others are frustrated that they have been unsuccessful at extorting money from CMS. Whether or not these allegations are true, Osei clearly opposes this deal, has the ear of the President, and refuses to be dissuaded from his arguments. Post will continue to support CMS and IFC in educating GoG Ministers and building support in Cabinet for the deal, and will encourage CMS to be more assertive in correcting misperceptions. IFC flexibility is clearly needed in order to gain Kufuor's support for the project. End Comment.
BRIDGEWATER